PHILIPPINES ECONOMIC WRAP-UP
FEBRUARY 10-16, 2001

Summary

The rehabilitation and reopening of Urban Bank appears to have been derailed by allegations of the bank's connections to former President Estrada. Other bank mergers, however, continue to move forward. The continued deferral of the "Expanded Value Added Tax" on financial and other services will give the government and legislature more time to decide how to define "value added." While exports in 2000 continued to grow, they grew far below expectations. And we report on a few key developments growing out of the opening of the retail trade sector to foreign investment.

These weekly reviews are available on the Embassy's web site (http://usembassy.state.gov/manila). We provide a longer and more detailed review of the Philippine economy in our February 2001 Economic Outlook, which is also available on our web site.

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Market and Policy Developments

FOREX REPORT

The Philippine peso continued to strengthen against the dollar this week. Traders suggested that dollars were continuing to flow into the Philippines based on hopes that the new government would be able to push forward with a real agenda for reform, creating new business opportunities. On moderate trading activity, the peso strengthened to close at P47.55/US$ from its February 9 close of P48.20/US$.

Exchange Rate Tables

Date	Weighted Average (Pesos/US$)	Closing (Pesos/US$)	Volume (Million US$)
JAN 08	50.939	50.940	93.0
09	50.902	50.935	77.0
10	51.064	51.150	112.0
11	51.325	51.325	149.5
12	51.460	51.590	99.6
JAN 15	51.978	52.400	134.1
16	52.649	52.780	158.0
17	54.808	54.625	70.0
18	55.013	54.790	118.5
19	53.357	47.500	101.6
JAN 22	48.207	49.300	188.3
23	49.750	49.200	122.2
24	48.473	48.350	150.0
25	48.638	48.840	116.0
26	49.321	49.720	124.3
JAN 29	49.676	49.480	126.0
30	49.412	49.600	110.6
31	49.221	48.975	99.4
FEB 01	49.150	49.160	168.0
02	49.215	49.120	118.0
FEB 05	49.161	49.110	62.5
06	48.857	48.610	161.0
07	48.706	48.580	139.1
08	48.284	48.250	187.5
09	48.052	48.200	120.6

FEB 12	48.140	47.820	167.5
13	47.674	47.630	131.1
14	47.583	47.955	131.0
15	47.889	47.490	267.5
16	47.550	47.550	125.6

Source: Bankers Association of the Philippines

CREDIT MARKET REPORT

On expectations that the policy making Monetary Board of the Bangko Sentral ng Pilipinas (BSP, the central bank) will continue to cut its key policy rates (and suggestions the U.S. Federal Reserve will do the same), interest rates in the Philippines continue to moderate. The Monetary Board announced another 50 basis point cut in overnight rates on February 9, bring the borrowing and lending rates to 11% and 13.25% respectively. This is the fifth such cut since the beginning of the year.

With more than P10 billion worth of bids chasing P4 billion worth of T-bills on offer at the February 12 action, interest rates on 91-day bills dropped 25.6 basis points to 10.607%. Rates on the 182-day bill fell 26.1 basis points to 11.913%; but rates on the 364-day bill only eased 6.2 basis points to 12.632%. At the auction of 2-year Treasury bonds on February 10, the interest rate on the bonds sank 50 basis points to 13.625%. A full award of P3 billion was made against over P7 billion worth of bids.

Department of Finance Undersecretary Joel Banares told reporters that the government planned a $400 million bond float sometime later this year, probably after May 2001 elections. Banares said the amount could be increased, but that the timing of the roadshow to promote the bonds would wait until June. Banares said the delay would allow the government to have some more concrete results to show potential investors, including a completed electric power reform package, resulting in lower borrowing costs.

Domestic Interest Rates (in percent)

Treasury Bills

Auction Date	91 days	182 days	364 days
JAN 08	12.598	13.657	14.240
JAN 15	12.365	13.657	14.237
JAN 22	11.760	12.556	13.136
JAN 29	11.165	12.181	12.699
FEB 05	10.863	12.174	12.694
FEB 12	10.607	11.913	12.632

Source: Bureau of the Treasury

Prime Lending Rates of 15 Expanded Commercial Banks

Date of Survey	Average	Range
JAN 11	17.1677	14.50 – 20.00
JAN 17	17.1154	14.50 – 21.00
JAN 25	16.8757	13.50 – 20.00
FEB 01	16.4046	12.75 – 20.00
FEB 08	15.8376	12.50 - 19.00
FEB 15	15.2550	12.25 – 19.00

Sources: Bangko Sentral ng Pilipinas; Press reports

STOCK MARKET REPORT

The Philippine stock market just held its own this week. Traders said that a lack of any significant good corporate news kept major investors away. What trading activity there was was driven by profit taking and bargain hunting. From its February 9 close of 1695.59, the 33-share Philippine Stock Index fell marginally to close at 1689.91.

Philippine Stock Exchange Index (PHISIX) and Value of Shares Traded

Date	PHISIX Close	Value (Million pesos)
JAN 08	1494.38	522
09	1531.82	682
10	1534.15	962
11	1515.89	609
12	1541.65	798
JAN 15	1567.93	1910
16	1551.79	1359
17	1458.63	1876
18	1438.21	1114
19	1452.93	1204
JAN 22	1708.06	7161
23	1662.30	2724
24	1665.43	1153
25	1639.18	877
26	1708.18	6074
JAN 29	1686.28	1319
30	1668.43	728
31	1687.00	1159
FEB 01	1669.13	601
02	1669.58	616
FEB 05	1652.08	352
06	1664.23	652
07	1659.25	441
08	1683.44	764
09	1695.59	995
FEB 12	1712.06	734
13	1692.27	556
14	1687.74	622
15	1688.05	534
16	1689.91	950

Source: Philippine Stock Exchange

PHILIPPINE ECONOMIC OUTLOOK RELEASED

The U.S. Embassy has released its February 2001 Philippine Economic Outlook. The 12 page report constitutes a broad overview of recent economic events, as well as informal analysis of challenges facing the new government of President Macapagal-Arroyo. The document also includes charts, graphs, and a full page of vital economic statistics. The report is now available on the Embassy Internet website at:
http://usembassy.state.gov/manila.

BANK NOTES

Bank Merger Sinks Deeper into Limbo: As a "sequel" to our report last week, the much-awaited merger between Bank of Commerce (BOC) and Urban Bank (a medium-sized commercial bank which closed in April 2000) appears to have been thrown into even deeper uncertainty. Last week, a BOC statement said that the bank remained committed to the merger, even as it "considered it prudent to proceed only if all legal issues are resolved with finality". A statement this week, however, indicates that BOC may be heading for a complete change of heart. That statement said "an assessment of recent developments makes it necessary for BOC to reconsider this line of direction [sic]." BOC's president stated that "the paramount question in our minds is if it is still viable for BOC to merge with Urban Bank considering the controversy the closed bank has generated recently."

In addition to the escalating legal battle between the Bangko Sentral and former Urban Bank officials over the latter's closure, recent weeks saw former congressmen, who served as prosecutors in the aborted impeachment trial, linking Urban Bank to alleged Estrada accounts. They claimed that the former Philippine president had been able to withdraw funds from Urban Bank –- possibly funded by interbank loans from a government bank –- just before Urban Bank declared a bank holiday. They also accused BSP Governor Rafael Buenaventura (an Estrada appointee with a fixed six-year term) of having used advance knowledge to tip off the former Philippine president as well as the BSP Provident Fund.

Less than two weeks ago, BOC appeared all set to implement the merger -- confirming to Embassy that it was merely waiting for the Bangko Sentral's official go-ahead after having obtained the approval of Urban Bank's depositors and creditors. Senior officials at the Bangko Sentral and Philippine Deposit Insurance Corporation had also indicated that they expected Urban Bank to reopen (under BOC management) before the end of the quarter. In his most recent statement this week, however, BOC's president said "we want the viability of the merger to be assured and anything less than this will naturally require us to re-study our options."

But More Bank Mergers in the Works: The Monetary Board (the Bangko Sentral's highest policymaking body) recently approved a merger between commercial banks Banco de Oro (controlled by taipan Henry Sy) and Dao Heng Bank (local subsidiary of the Hong Kong-based Dao Heng Bank group). Banco de Oro officials said the two banks had signed a memorandum of understanding to merge before December 2000. As of end-2000, Banco de Oro ranked thirteenth (by assets) among the 45 commercial banks in operation, and Dao Heng Bank forty-first. According to industry reports, the merger will be executed through a share swap arrangement (where Dao Heng Bank ends up with a minority interest in Banco de Oro).

The Monetary Board also approved a merger between commercial bank Philippine Bank of Communications (PBCom, eighteenth largest in terms of assets) and Consumer Savings Bank (a thrift bank). PBCom officials said an agreement between the two banks had been reached in November.

There are another 18 acquisition or merger proposals (involving 3 commercial banks, 4 thrift banks, 30 rural banks, and 1 non-bank financial intermediary) pending BSP approval. Since the Asian crisis, the Bangko Sentral has approved 31 acquisition or merger arrangements (involving 26 commercial, 16 thrift, 6 rural banks, as well as 8 non-bank intermediaries).

EVAT ON BANKING AND OTHER SERVICES TO BE DEFERRED ANEW
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President Gloria Macapagal-Arroyo is expected to sign into law a bill which will defer to January 2003 the imposition of a 10% value-added tax on services rendered by banks and other non-bank financial intermediaries. The bill, ratified by both houses of Congress before adjourning on February 8, also defers the imposition of the 10% VAT on the practice of professions; on services rendered by broadcasting, cinematographic, and other media talents; and on professional athletes. These services were among those included for VAT coverage under an "expanded value added tax" (EVAT) law signed in 1994. The EVAT broadened the scope of the original 1988 VAT law, but provided for deferred effectivity (to January 1997) for the particular services mentioned above. Three more deferments (the last of which was supposed to have lapsed at the end of 2000) followed. The recently ratified bill would represent a fifth postponement.

The government's goal was to replace the long-criticized 5% gross receipts tax (GRT) imposed on most financial intermediaries with VAT. The VAT was also intended to replace a long-criticized 5% tax on life insurance premiums. However, issues subsequently arose on how "value added" should be determined for banks and financial services firms; hence the deferments. The government had been working on a more acceptable formula to determine value added for financial services (referred to as the "financial institution tax" or "FIT"). That effort has been the subject of often contentious consultations with industry players, as well as of delays caused by changes of leadership at the Department of Finance (DOF). DOF officials said that their agency had presented the latest version of the proposed FIT (together with a bigger financial tax reform package of which it is a part) to the Lower House's ways and means committee in September 2000. However, the DOF was unable to have the proposed legislation sponsored and filed. The government intends to resubmit a financial tax reform package to the new Congress which convenes in July.

DOF officials also told the Embassy that they expect a VAT on professional services to remain a contentious issue. In providing for the latest deferment, legislators had argued that the "exercise of a profession" was more a call to public service rather than a money-making pursuit (a claim which, not surprisingly, has met with considerable skepticism). The legislators had argued that the VAT –- a tax on the sale of goods and services “in the ordinary course of trade or business” –- therefore appeared inappropriate. Concerns have also been raised on the potential upward effect of a 10% VAT on professional fees (especially for essential services rendered by, for example, doctors and other medical practitioners).

2000 EXPORTS UP 8.7%, FAR BELOW 15% TARGET

Due to a substantial slowdown in global demand for electronics (from 23% in 1999, annual growth declined to 4.4% in 2000), which account for nearly 60% ($22.5 billion last year) of annual merchandise shipments, Philippine export growth year-on-year slipped from a strong 18.8% in 1999 ($35 billion) to 8.7% in 2000 ($38 billion) (table I). While this was well below an earlier growth target of 15% to $40 billion, some analysts say foreign buyers who stepped up 1999 orders ahead of the transition to the new millennium have been using their inventory. Industry sources have conceded that transfer prices of many electronic devices have rapidly gone down as existing models are rapidly replaced by new and improved-technology products in the market.

Other important exports such as automotive parts and accessories and garments, which posted two-digit growth rates of 19% (to $5.9 billion) and 12% (to $2.8 billion) respectively, also contributed to total 2000 export receipts (table II). Agricultural exports, led by coconut and fruits and vegetables, also posted two-digit growth rates, although their contribution accounted for just four percent of total export receipts. December’s strong performance (up 18.7% from a year-ago level) was attributed to a 20% rebound year-on-year in electronics exports. Despite strong growth in shipments of non-electronic products, the electronics sector will remain the economy’s main export driver.

Some industry analysts see the economic slowdown now being experienced by the U.S. and Japan as the biggest drag on Philippine exports. The U.S. remains the Philippines’ largest market particularly for semiconductor devices, garments, coconut oil and sugar.

The U.S. purchased $11.4 billion worth of Philippine products, accounting for 30% of the country's total exports in 2000. Japan is second largest market having purchased $5.6 billion worth of Philippine goods (led by electronics and automotive parts) or 15% of total shipments.

Table I
Philippine Export Performance
January – December 2000

	1999	2000	Pct Change
	(Value in Mill US$)		(y/y)
January	2,581	2,717	5.3
February	2,569	2,902	13.0
March	2,702	2,989	10.6
April	2,346	2,668	13.7
May	2,747	2,931	6.7
June	2,857	3,410	19.4
July	2,851	3,219	12.9
August	3,212	3,529	9.9
September	3,693	3,502	(5.2)
October	3,460	3,398	(1.8)
November	3,075	3,317	7.9
December	2,944	3,495	18.7
Jan-Dec	35,037	38,077	8.7

Source: National Statistics Office

Table II
Major Philippine Exports
January - December 2000

	1999	2000	Growth Rate
	(Value in Mill US$)		(in pct)
TOTAL EXPORTS	35,037	38,077	8.7
Manufactures	31,734	34,363	8.3
Electronic Eqpmt. & parts	21,558	22,517	4.4
Mach. & Transport Eqpmt.	4,971	5,930	19.3
Garments & Textiles	2,489	2,801	12.5
Other Manufactures	2,716	3,115	14.7

Agro-based Products	1,461	1,656	13.3
Coconut Products	458	569	24.2
Fruits & Vegetables	456	535	17.3
Shrimp and Prawns	287	328	14.3
Other agro-based	260	224	(13.8)
Mineral Products	645	649	0.6
Other Traditional	816	1,007	23.4
Other Transactions/re-exports	956	932	(2.5)

Source: National Statistics Office

RETAIL TRADE SECTOR EXPANDS

Following Price Smart's announcement to independently open its first retail store in the Philippines, US-based Wal-Mart Inc. has confirmed its planned entry into the local retail business (its first venture in Asia) after it backed out late last year citing political uncertainty. Trade and Industry Secretary Manuel A. Roxas has asserted that Wal-Mart is finalizing its entry strategy, whether to do a solo (like Price Smart) or enter the market with a partner (like President group of Taiwan). Wal-Mart is looking at possibly breaking ground for its first retail store (Sam's Club type) by third quarter of this year. Wal-Mart is also looking into establishing a regional distribution and training center in view of the country's large pool of English-speaking and skilled workers. Wal-Mart will be the third major foreign retailer to come into the country since the retail trade industry was liberalized last year.

On February 9, the Gokongwei family's Robinson Retail Group opened its first outlet of a convenience-store chain designed to compete with market leader 7-Eleven. Called "Mini Stop", Robinson's latest venture is a P400-million (about $8.5 million) tie-up with Japan's Mitsubishi Corp. (40%) and Mini Stop Corp. Ltd. (4%). Robinson's goal in the next three to five years is to put up over 500 combo-store and fast-food outlets where customers will be able to pay their electricity, water and phone bills (utility bills) through Mini Stop stores. Mini Stop is Robinson’s second venture with Mitsubishi; the first is Nissin’s noodle production.